FINLAND

The Department of State submitted this report to the Senate Committees on Foreign Relations and on Finance and to the House Committees on Foreign Affairs and on Ways and Means, on January 31, 1999.

Key Economic Indicators

(Billions of U.S. Dollars unless otherwise indicated)

	1996	1997	1998	
Income, Production and Employment:				
Nominal GDP (at factor cost) 9/	108.6	103.7	109.4	1/
Real GDP Growth (pct)	3.6	6.0	5.1	1/
GDP by Sector:				
Agriculture, Forestry & Logging	4.4	4.2	4.2	1/
Manufacturing, Construction, Mining & Quarrying	34.3	34.4	37.0	1/
Electricity, Gas & Water Supply	3.0	2.7	2.7	1/
Services	46.6	44.1	47.0	1/
Government	20.9	19.1	19.1	1/
Other Activities	2.3	2.1	2.1	1/
Imputed Bank Service Charges	-2.9	-2.9	-2.7	1/
Per Capita GDP (US$) 9/	24,520	23,150	23,602	1/
Labor Force (000s)	2,490	2,488	2,490	1/
Unemployment Rate (pct) 10/	14.6	12.7	11.4	1/
Money and Prices (annual percentage growth):				
Money Supply Growth (M2)	-2.0	1.0	4.4	2/
Consumer Price Inflation	0.6	1.2	1.5	1/
Exchange Rate (FIM/US$ annual average)	4.59	5.19	5.30	3/
Balance of Payments and Trade:				
Total Exports FOB	40.5	40.7	28.7	4/
Exports to U.S.	3.2	2.8	2.1	4/
Total Imports CIF	30.7	30.7	21.5	4/
Imports from U.S.	2.2	2.3	1.8	4/
Trade Balance	9.8	10.0	7.2	4/
Balance with U.S.	1.0	0.5	0.3	4/
External Public Debt 5/	-37.6	-29.8	-21.3	1/
Fiscal Deficit-Surplus/GDP (pct) 7/	-3.5	-1.1	1.2	1/
Current Account Surplus/GDP (pct)	4.0	5.5	5.8	1/
Debt Service Payments/GDP (pct) 6/	5.8	5.4	5.1	1/
Gold and Foreign Exchange Reserves	7.9	9.9	8.7	8/
Aid from U.S.	N/A	N/A	N/A	
Aid from All Other Sources	N/A	N/A	N/A	

1/ Estimate, Ministry of Finance.
2/ September 1997 - September 1998.
3/ January-September 1998, Bank of Finland middle rate.
4/ January-August 1998, Board of Customs.
5/ Net international investment position exc. shares and other equity items.
6/ General government interest expenditures.
7/ Public sector's budget deficit (EMU).
8/ September 1998, Bank of Finland.
9/ Declines in Nominal and Per Capita GDP (despite positive growth rates) are due to the depreciating value of the Finnish Markka.
10/ According to the new, revised labor force study.

1. General Policy Framework

At the beginning of the 1990's, the Finnish economy encountered a severe recession, after a period of rapid growth in the 1980's. GDP growth came to a standstill in 1990 and the following year declined by 7 percent. Industrial output and exports bottomed out in 1991, and total industrial output did not start to grow again until 1993. Unemployment has decreased significantly since 1994, but remains above the European Union (EU) average. EU membership, which took place on January 1, 1995, helped spur structural change in key economic sectors.

Economic growth remained strong throughout the first half of 1998, with particularly robust growth in industrial production and construction. With the deepening of the Asian and Russian economic crises, the growth rate is expected to decelerate towards the end of 1998. Nevertheless, total output is forecast to grow 5.1 percent in 1998 and 3.6 percent in 1999. Inflation is anticipated to remain low in 1998. Wage increases, moderate as such, were the main factor behind minimal rise in costs.

Public sector revenues are expected to grow in 1998, due to increasing tax revenues and curbed growth in expenditures. The financial deficit, as calculated in the national accounts, suggests a fall of almost 2 percentage points relative to GDP, down to 2.5 percent. State debt is anticipated to rise in terms of total value, but as a proportion of GDP it is set to fall to 63.4 percent by the end of 1998, having peaked at 68.9 percent in 1996. Local government finances are forecast to be close to balance in 1998. The strengthening of public sector revenues puts the government budget in the surplus for the first time since 1990. The public sector EMU debt as a proportion of GDP is predicted to fall below 51 per cent by the end of 1998.

According to the Ministry of Finance's 1998 stability program, Finland's public sector is projected to show a surplus of 1.2 percent as a percent of GDP in 1998, and in 2001 there should be a 2.1 percent budget surplus with a debt/GDP ratio of 44.8 percent. It is expected that total public debt (gross debt EMU) for 1998 will amount to about 50.9 percent of GDP, well within the EMU criteria of 60 percent.

In 1997 Finland's tax ratio (gross wage-earner taxation, including compulsory employment pension contributions, relative to GDP) was down to 47 percent from 48.1 percent in 1996. A marginal rise is expected in 1998 (47.1 percent) and a fall of 0.6 percentage point is predicted for 1999 to 46.5 percent.

Debt servicing accounted for 17 percent of government expenditures in 1997. Modest cuts in government social programs and aid to municipalities are helping to keep the debt from rising even faster.

Despite high levels of foreign debt servicing, Finland's balance of payments outlook remains good. Finland has maintained a current account surplus since 1994. The 1997 current account surplus of $6.6 billion is expected to rise to about $7.4 billion in 1998 (6.2 percent of total output). The surplus in merchandise trade in 1998 is expected to rise to $11 billion. In 1999, the terms of trade are envisaged to remain at 1998's level.

Finnish economic policy is determined to a large extent by consultation and coordination within the EU. EU membership, for example, has resulted in new competition legislation that could help to reduce the cartelized nature of many Finnish industries. Legislation which took effect at the beginning of 1993 liberalizing foreign investment restrictions has helped spur a sharp increase in foreign portfolio investment and hence has contributed to the internationalization of large Finnish companies. The increase in stock market activity is also due to lower domestic interest rates. Direct foreign investment, however remains modest due to high production costs. Finland is hoping to capitalize on its location and expertise to serve as a gateway for foreign investors in the former Soviet Union and the Baltic States. This effort had scored some successes as foreign firms established production and warehousing facilities in eastern Finland, close to the major Russian markets. The recent Russian financial crisis has caused a significant slowdown in gateway activity.

EU membership and Finland's budget constraints have brought about some reform in Finland's highly protected agricultural sector. Finland is slowly transitioning to the EU agricultural regime. The EU agreed to pay compensation totaling approximately $585 million through 1999 for the decrease in value of agricultural stocks and other costs associated with Finland joining the EU. Finland was also granted permission to pay national adjustment support for five years until year 1999. However, these support mechanisms will not be adequate to prevent major structural changes in the agricultural sector. Over the long run, structural changes will entail a reduction in the number of farmers and the consolidation of surviving farms into larger, more efficient units.

In 1996, producer prices for agriculture fell more in Finland than in any other EU country. In 1997 food prices averaged 11.2 percent lower than in 1994 (prior to Finland's EU membership). This fall in prices has been caused by producers reducing prices to EU levels and by intensified competition from EU agricultural imports. So far, most Finnish producers have maintained their domestic market shares, but at the cost of significantly lower profits. In 1997, agricultural output climbed by just under 8 percent, as grain production increased considerably, due to favorable weather. Agricultural output is expected to fall significantly in 1998 due to adverse weather conditions, which depressed the production of grain substantially.

2. Exchange Rate Policy

A 1996 amendment to the Currency Act provides the legislative basis for Finland's participation in the Exchange Rate Mechanism (ERM) of the European Monetary System. As of 16 March 1998, the ECU central rate is FIM 6.01125. As a participant in the ERM, Finland takes part in the mutual intervention arrangements coordinated between the various central banks, which contribute to economic policy goals by stabilizing the exchange rate.

The European Commission reported on 25 March 1998, that 11 EU member countries, one of them Finland, were ready for the economic and monetary union (EMU) and met the conditions to adopt the single currency (Euro). Stage three of the EMU commences at the beginning of 1999. The bank notes and coins of the single currency will be put into circulation in

2002. The irrevocably fixed conversion rates of the national currencies against the Euro will be fixed at the launch of stage three on January 1, 1999.

3. Structural Policies

Finland replaced its turnover tax with a Value-Added Tax (VAT) in June 1994. While the change has had little effect on overall revenues, several sectors not previously taxed or taxed at a lower rate, including corporate and consumer services and construction, are now subject to the new VAT. The government has kept the basic VAT rate at the same level as the old turnover tax (22 percent). Legislation on VAT was harmonized with the European Union. Foodstuffs will still be taxed at a 17 percent rate. Services, including health care, education, insurance, newspaper & periodical subscriptions, and rentals are not subject to VAT.

Agricultural and forestry products continue to be subject to different forms of non-VAT taxation. A uniform tax rate of 28 percent on capital gains took effect in 1996, which includes dividends, rental income, insurance, savings, forestry income, and corporate profits. The sole exception was bank interest, where the tax rate was increased from 20 to 25 percent at the beginning of 1994.

In March 1997, European Union commitments required the establishment of a tax border between the autonomously governed, but territorially Finnish, Aland Islands (Ahvenanmaa) and the rest of Finland. As a result, the trade of goods and services between the rest of Finland and Aland is now treated as if it were trade with a non-EU area. The trade effect of this treatment is minimal since the Aland Islands are part of the EFTA tariff area.

The structure of taxation has been revised to expand employment opportunities and make work pay. The income brackets in all state income tax scales are to be raised by 2 percent in 1999, and all marginal income tax percentages except the top bracket will be lowered by 0.5 percentage points. Even with this reduction, however, the tax/GDP ratio will remain at historically high levels.

An income policy agreement contract was signed on 12 December 1997 by the Finnish central labor market organizations, which covers all wage and salary earners and is effective until 15 January 2000. The cost effect of the pay increases included in the agreement will be on average 2.6 percent as calculated from the beginning of 1998, including a general increase of 1.7 percent. Following a further general increase at the beginning of 1999 wages will increase by an average of 1.7 percent.

Trade unions publicly have affirmed the importance of keeping inflation under control (The Bank of Finland's target is 2 percent), as well as maintaining the competitiveness of Finnish industry. Given these goals, increases in labor costs over the next two years should be fairly low.

To offset reductions in income tax the Finns have raised "environmental taxes" on some energy resources.

The sharp decline in interest rates and liberalization of foreign investment has resulted in a strong revival of the Finnish stock market and greater corporate use of equity markets. It has also substantially increased the percentage of foreign ownership of many of Finland's leading companies, and is the preferred vehicle for privatization or partial privatization of companies with significant state ownership. The previous Center-Conservative government initiated a program aimed at privatizing as much of the state-owned companies as the Finnish Parliament would permit and the market could absorb. The present government agrees that state ownership at its present level is no longer necessary in manufacturing and energy production. The basic strategy has been to reduce the government's stake through the issuance of stock, rather than by selling off companies to individual investors. In every case, however, the State has retained a substantial minority holding which ensures that the State will remain the largest shareholder.

Currently, three of Finland's ten largest companies are majority state-owned, Neste (83.5 percent), Outokumpu (40 percent) and Kemira (53.8 percent). Since 1993 the state has reduced its ownership in 13 state companies. The Finnish Parliament voted in favor of abolishing the rule concerning the State's one third minority share holding in Enso. The direct holding of the State will be slightly less than 18 percent of the shares and approximately 21 percent of the voting rights. The state intends to continue its privatization program and is presently privatizing its tele-operations corporation Sonera. In the current offering, the state sold 22 percent of Sonera and will reduce its stake to 50.1 percent at a later date. The government is also to go ahead with partial privatization of the Neste oil and IVO power generation combine called Fortum, with an initial offering at the end of November 1998. There are 24 companies in Finland with varying degrees of state ownership.

As a result of the recession of the early 1990s, industrial subsidies have increased by about 80 percent of GDP in real terms. The government has begun, however, to reduce subsidies in line with the need for greater fiscal discipline and Maastricht Treaty criteria for monetary union. General horizontal subsidies form the bulk of aid in Finland, including assistance for research and development, environmental protection, energy and investment. All companies registered in Finland have access to government assistance under special development programs. Foreign-owned companies are eligible for government incentives on an equal footing with Finnish owned companies. Government incentive programs are mainly aimed at investment in areas deemed to be in need of development. The support consists of cash grants, loans, tax benefits, investments in equity, guarantees and employee training.

4. Debt Management Policies

Since the early 1990's Finland has rapidly accumulated external debt in order to finance recession-induced budget deficits. Under the government's EMU convergence program, the general government debt is projected to drop to 47.2 percent of GDP by 1999. Finnish corporations, formerly heavy users of foreign capital, are now reducing foreign obligations. However, financing requirements of the central government have not diminished significantly.

In May 1998, Moody's upgraded its rating on Finnish long-term government bonds to their best rating -- Aaa. Standard & Poor's rating was upgraded in December 1996 to AA, which is the third best. Finnish debt issues continue to sell easily in international financial markets.

Finland is an active participant in the Paris Club, the London Club and the Group of 24, providing assistance to East and Central Europe and the former Soviet Union. It has been a member of the IMF since 1948. Finland's development cooperation programs channel assistance via international organizations and bilaterally to a number of African, Asian, and Latin American countries. In response to budgetary constraints and changing priorities, Finland has reduced foreign assistance from 0.78 percent of GDP in 1991 to 0.34 percent of GDP in 1998. The Finnish Government intends to raise foreign assistance to 0.4 percent of GDP by year 2000.

5. Significant Barriers to U.S. Exports

Finland became a member of the EU in 1995, and, as a result, has had to adopt the EU's tariff schedules. The agricultural sector remains the most heavily protected area of the Finnish economy, with the bulk of official subsidies in this sector. The amount of these subsidies is determined by the difference between intervention and world prices for agricultural products. Since joining the EU, the difference between these two prices has decreased for most agricultural items, resulting in lower, albeit still significant, subsidy levels. As part of its terms of EU accession, Finland temporarily imposes higher tariffs than EU levels on the following items: footwear, rubber, plastic, metals, raw hides and skins and some electric machinery. This transition period ends in 1998.

In mid-1996 the Finnish government's inter-ministerial licensing authority began to oppose within the EU U.S. company applications for commercialization of genetically modified organisms (GMOs) such as insect resistant corn. The Environmental Ministry appears to favor mandatory consumer-oriented labeling of GMOs. Other ministries are more supportive of GMO commercialization. The government continues to take a case-by-case approach to GMO-related issues.

The Finnish service sector is undergoing considerable liberalization in connection with EU membership. Legislation implementing EU insurance directives have gone into effect. Finland has exceptions in insurance covering medical and drug malpractice and nuclear power supply. Restrictions placed on statutory labor pension funds, which are administered by insurance companies, will in effect require that companies establish an office in Finland. In most cases such restrictions will cover workers' compensation as well. Auto insurance companies will not be required to establish a representative office, but will have to have a claims representative in Finland.

1995 was the first year of fully open competition in the telecommunications sector in Finland. The Telecommunication Act of August 1996 allows both network operators and service operators to use competitor telecommunication networks in exchange for reasonable compensation. The Telecommunication Act was replaced by the Telecommunications Market Act of 1997, which improved the opportunities of telecommunication operators to profitably lease each other's telecommunications connections. Entry to the sector was also made easier, by eliminating a licensing requirement to construct a fixed telephone network. Only mobile telephone networks are still subject to license.

The government requires that the Finnish broadcasting company devote a "sufficient" amount of broadcasting time to domestic production, although in practical terms this has not resulted in discrimination against foreign produced programs. Finland has adopted EU broadcasting directives, which recommend a 51 percent European programming target "where practicable" for non-news and sports programming. Finland does not intend to impose specific quotas and has voiced its opposition to such measures in the EU.

With the end of the Restriction Act in January 1993, Finland removed most restrictions on foreign ownership of property in Finland. Only minor restrictions remain, such as requirements to obtain permission of the local government in order to purchase a vacation home in Finland. But even restrictions such as this will be abolished as by January 2000, bringing Finland fully in line with EU norms.

Foreigners residing outside of the EEA who wish to carrying on trade as a private entrepreneur or as a partner in a Finnish limited or general partnership must get a trade permit from the Ministry of Trade and Industry (MTI) before starting a business in Finland. Additionally, at least one-half of the founders of a limited company must reside in the EEA unless the MTI grants an exemption.

Normally Finland requires that a labor market test be conducted before allowing a foreigner to work in Finland. The purpose of the test is to determine whether or not the same work could be undertaken by a Finn. However, foreign intra-corporate transferees who are business executives or managers are not subject to the labor market test. This standard does not apply to company specialists, who must prove that they possess knowledge at an advanced level of expertise or are otherwise privy to proprietary company business information.

Finland is a signatory to the WTO Government Procurement Agreement and has a good record in enforcing its requirements. In excluded sectors, particularly defense, counter trade is actively practiced. Finland is purchasing fighter aircraft and associated equipment valued at $3 billion from U.S. suppliers. One hundred percent offsets are required, as a condition of sale, by the year 2005. As of October 1997, $2.7 billion (or 80 per cent of the total) worth of offsets have been made.

Finland has in most cases completed the process of harmonizing its technical standards to EU norms. It has streamlined customs procedures and harmonized its practices with those of the EU.

6. Export Subsidies Policies

The only significant Finnish direct export subsidies are for agricultural products, such as grain, meat, butter, cheese and eggs as well as for some processed agricultural products. Finland has advocated worldwide elimination of shipbuilding subsidies through the OECD Shipbuilding Agreement. It is presently debating whether or not to become the first European Union country to abandon shipyard subsidies as of 1999, two years before the EU eliminates them.

7. Protection of U.S. Intellectual Property

The Finnish legal system protects property rights, including intellectual property, and Finland adheres to numerous international agreements and organizations concerning intellectual property. In 1996, Finland joined the European Patent Convention (EPC).

Finland is a member of WIPO, and participates primarily via its membership in the EU. The idea of protection of intellectual property is well developed. For example, the incidence of software piracy is lower than in the U.S., and by some measures (e.g. BSA) is the lowest in the world.

The Finnish Copyright Act, which traditionally also grants protection to authors, performing artists, record producers, broadcasting organizations and catalog producers, is being amended to comply with EU directives. As part of this harmonization, the period of copyright protection was extended from 50 years to 70 years. Protection for data base producers (currently a part of catalog producer rights) will be defined consistent with EU practice. The Finnish Copyright Act provides for sanctions ranging from fines to imprisonment for up to two years. Search and seizure are authorized in the case of criminal piracy, as is the forfeiture of financial gains. Computer software has been covered by the Copyright Act since 1991.

Information on copying and copyright infringement is provided by several copyright holder interest organizations such as the Copyright Information and Anti-Piracy Center. The Business Software Alliance (BSA), a worldwide software anti-piracy organization, began operations in Finland in January 1994. According to a BSA survey, the rate of software piracy in Finland dropped to 38 percent in 1997, from 53 percent in 1994. The average software piracy rate in Western Europe was 39 percent in 1997.

8. Worker Rights

a. The Right of Association: The constitution provides for the rights of trade unions to organize, to assemble peacefully, and to strike, and the government respects these provisions. Over 80 percent of the work force are organized. This applies to employers as well. All unions are independent of the government and political parties. The law grants public sector employees the right to strike, with some exceptions for provision of essential services. In the fourth quarter of 1997, there were 18 strikes, one of which, the firemen's strike, was not a wildcat strike. Trade unions freely affiliate with international bodies.

b. The Right to Organize and Bargain Collectively: The law provides for the right to organize and bargain collectively. Collective bargaining agreements are usually based on incomes policy agreements between employee and employer central organizations and the government. The law protects workers against antiunion discrimination. Complaint resolution is governed by collective bargaining agreements as well as labor law, both of which are adequately enforced. There are no export processing zones.

c. Prohibition of Forced or Compulsory Labor: The Constitution prohibits forced or compulsory labor, and this prohibition is honored in practice.

d. Minimum Age for Employment of Children: Youths under 16 years of age cannot work more than 6 hours a day or at night, and education is compulsory for children from 7 to 16 years of age. The Labor Ministry enforces child labor regulations. There are virtually no complaints of exploitation of children in the work force. In 1998, a proposal to tighten the law even further has been made. According to a bill introduced to parliament, comprehensive school student (7-15 years) should not be allowed to hold employment during two thirds of the their holidays, but only during one half. This change is prompted by an EU directive to this effect.

e. Acceptable Conditions of Work: There is no legislated minimum wage, but the law requires all employers, including non-unionized ones, to meet the minimum wages agreed to in collective bargaining agreements in the respective industrial sector. These minimum wages generally provide a decent standard of living for workers and their families. The legal workweek consists of 5 days not exceeding 40 hours. Employees working in shifts or during the weekend are entitled to a 24-hour rest period during the week. The law is effectively enforced as a minimum, and many workers enjoy even stronger benefits through effectively enforced collective bargaining agreements. The government sets occupational health and safety standards, and the Labor Ministry effectively enforces them. Workers can refuse dangerous work situations, without risk of penalty.

f. Rights in Sectors with U.S. Investment: There is no difference in the application of worker rights between sectors with U.S. investment and those without.

Extent of U.S. Investment in Selected Industries -- U.S. Direct Investment Position Abroad on an Historical Cost Basis -- 1997

(Millions of U.S. Dollars)

Category	Amount	
Petroleum		(1)
Total Manufacturing		765
Food & Kindred Products	8	
Chemicals & Allied Products	258	
Primary & Fabricated Metals	18	
Industrial Machinery and Equipment	14	
Electric & Electronic Equipment	(1)	
Transportation Equipment	(1)	
Other Manufacturing	91	
Wholesale Trade		267
Banking		20
Finance/Insurance/Real Estate		(1)
Services		91
Other Industries		49
TOTAL ALL INDUSTRIES		1,338

(1) Suppressed to avoid disclosing data of individual companies.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.